# THE MONTH IN WASHINGTON

CalPERS

A Federal Report Provided by LGV&A

## FEBRUARY 2009

It was a busy first full month in office for President Obama. He signed into law a $787 billion economic stimulus bill, as well as $60 billion legislation to extend and expand the State Children's Health Insurance Program; he released a 10-year budget forecast that revealed some of his plans for health care reform; and he made several moves to increase accountability in the financial markets. Nearly all of his efforts, though, have been strongly resisted by most congressional Republicans, suggesting that talk of a new era of bipartisanship was probably just wishful thinking, and that the political battles to come – particularly those concerning health care reform – are likely to be as bitter as ever.

## ISSUES AND EVENTS

### *Obama Unveils More of Health Care Reform Plan*

President Obama announced a few more of his plans for health care reform in late February, including creation of a reserve fund to be used to expand coverage over the next decade. Obama proposed setting aside $634 billion to pay for health coverage for some of the 46 million Americans who now have none, though he provided no details of how the coverage is to be provided. About half of the money would come from increased taxes on the wealthy and a third from eliminating federal subsidies for Medicare Advantage plans. In addition, the plan would increase by nearly 50 percent the amount that pharmaceutical companies pay in rebates on drugs sold to Medicaid patients, charge wealthier senior citizens more for Medicare drug coverage and change certain rules regarding payments by Medicare and Medicaid. Obama also supported allowing the approval and manufacture of generic biologic drugs and preventing brand-name drug companies from entering into "pay-not-to-play" agreements with generic companies that keep generic drugs off the market.

The reserve fund, according to Peter Orszag, director of the Office of Management and Budget, would represent a "very substantial down payment" toward Obama's goal of universal health coverage. It is unclear, though, how much more money would be needed.

Drew Altman, president of the Kaiser Family Foundation, acknowledged the significance of both Obama's proposal and the unknown price tag that remains.

"What this does is, it allows the train to move forward," Altman said. "But there are still big issues to work out about how to reform health care and how to come up with the rest of the money."

The foundation on Feb. 25 released the results of a survey that found that more than half of Americans cut back on health care services because of cost concerns during the past year and that nearly 20 percent had suffered significant financial problems because of medical expenses.

Obama's proposals followed several legislative wins on health care in the first five weeks of his administration, including extension and expansion of the State Children's Health Insurance Program. The $60 billion "Children's Health Insurance Program Reauthorization Act of 2009" allows states to cover legal immigrants without the five-year waiting period that the program had required and increases the number of children eligible for the program from 7 million to more than 11 million. In addition, it mandates that states include dental coverage and equal treatment for mental and physical ailments in their SCHIP-funded programs. The $33 billion cost of the program expansion is to be funded by a 62-cent increase in federal tobacco taxes.

While Obama hailed the legislation as "a down payment on my commitment to cover every single American," some Republicans called it a move toward "socialized medicine," in part because the 11 million children now eligible for coverage include 2.4 million who would otherwise be expected to have private insurance. Rep. Tom McClintock, R-Calif., said SCHIP is "slowly replacing employer health plans with government-paid health plans, with spiraling costs to taxpayers."

The $787 billion economic stimulus bill, meanwhile, included several smaller-scale health care measures, such as $19 billion for health information technology improvements, $10 billion for biomedical research, $1.1 billion for comparative effectiveness studies and $1 billion for prevention and wellness programs. CalPERS Board President Rob Feckner and Chief Executive Officer Anne Stausboll wrote to House and Senate leaders in February to thank them for including some of CalPERS health care priorities in the legislation.

Obama's pursuit of health care reform suffered a setback, though, when his choice to be secretary of the Health and Human Services (HHS) Department, former Senate majority leader Tom Daschle, withdrew his nomination because of a failure to pay $140,000 in taxes on time. Obama was expected to name Kansas Gov. Kathleen Sebelius as his new pick to head HHS and lead his reform efforts in early March.

The president's latest proposals – including the reserve fund plan – were part of a 10-year budget outline released on Feb. 26 that forecasts $3.6 trillion in spending and a $1.2 trillion deficit in fiscal year 2010 and $42.2 trillion in total spending and a $7.0 trillion combined shortfall from 2010 to 2019. The outline shows the annual deficit shrinking to $533 billion by 2013, then growing again until it reaches $712 billion in 2019. The national debt is now $10.9 trillion.

***House Panel Begins Pension Hearings; Public Plans to Get Look***

An influential California congressman indicated in late February that he may try to add another leg to the retirement funding stool as part of an examination of all aspects of the pension system, including public plans.

House Education and Labor Committee Chairman George Miller of California noted at his panel's Feb. 24 hearing on retirement security that two of the three legs are shaky – defined contribution plans "have become little more than a high stakes crap shoot" and defined benefit plans have been "unceremoniously frozen or terminated" by many companies. (Social Security, meanwhile, "has never looked better," he said.)

"We must … ask the difficult questions about the state of our nation's retirement system as a whole and look to see whether we need to create a new leg of retirement security," Miller said, without indicating what the new leg might look like.

More specifically, though, Miller stressed the need for 401(k) reforms, including the elimination of hidden fees and conflicts of interest. In short, he said, "The 401(k) needs to be more transparent, fair, and operated on behalf of the account holder, not Wall Street firms."

Another California member of the committee, Rep. Buck McKeon, the panel's ranking Republican, acknowledged that the defined contribution system could be improved, but cautioned that, "to the extent we focus on one side of the equation – the defined contribution side – we must not ignore the other. It may be tempting this morning to talk about the risks associated with defined contribution plans and how workers would be so much better off if they were all in defined benefit plans. I think that misstates the case."

Miller indicated that defined benefit plans would not be immune to the committee's scrutiny, saying, "It is the intent of the chair to have exhaustive hearings on defined benefit plans, public plans and other plans."

The Education and Labor Committee can be influential on pension issues through oversight hearings such as this one, but official jurisdiction belongs to the Ways and Means Committee, and the chairman of that panel appears also to be interested in looking more closely at pensions.

Ways and Means Chairman Charles Rangel, D-N.Y., has asked that Select Revenue Measures Subcommittee Chairman Richard Neal, D-Mass., hold hearings on pension matters related to the impending retirements of tens of millions of baby boomers.

In a letter to Neal, Rangel said the hearings would provide "pertinent information and ongoing dialogue as we prepare for possible reform measures designed to ensure that America's workers have a secured retirement."

"In reviewing our current retirement system," Rangel wrote, "we must be prepared to adequately address who bears the ultimate cost and related risk of a secured retirement; the role of meaningful transparency of various features of our private retirement system, professional management of retirement assets, and the protection of retirement assets for the ultimate beneficiaries – the American workers."

Neal, for several years, has been sympathetic to the concerns of state and local retirement systems such as CalPERS that do not participate in Social Security. In 2007, the Coalition to Preserve Retirement Security, a group that CalPERS helped to form to oppose attempts to impose mandatory Social Security coverage on public employees, honored Neal for his support.

### *Obama Wants Executive Compensation Caps; Congress Wants Tighter Ones*

Congress has imposed caps on executive compensation for financial institutions receiving federal aid that are even tighter than what President Obama wanted.

Obama sought to require that companies receiving the greatest amount of aid from the federal Troubled Asset Relief Program (TARP) limit the pay of their executives to no more than $500,000 each and provide no additional compensation besides company stock, which could only be redeemed after the company paid back the federal government.

The measure approved by Congress as part of the economic stimulus bill, though, limits executive bonuses – which often are a huge portion of the compensation package – to no more than a third of annual base salary and applies the rule to all firms receiving federal assistance. In addition, it would ban golden parachutes for top executives at those companies and require the firms to hold shareholder votes on executive compensation until the funds are repaid.

Some members of the financial industry have expressed concern that the rules could make it hard for troubled firms to keep and maintain talented executives. Nell Minow of the Corporate Library, a corporate governance research organization, has also cautioned that the limits could have unintended, negative consequences, perhaps making the timely repayment of government funds less likely. "The people who work on Wall Street are motivated by money," Minow said. "And we should make sure we hold that carrot in front of them until we get the last dime."

The president's press secretary, Robert Gibbs, has indicated that the administration plans to discuss possible changes to the executive compensation provision with members of the House and Senate. A key committee chairman, however, rejected that idea.

"Mr. Gibbs may not like it, but it is going to be enforced," House Financial Services Committee Chairman Barney Frank said. "This is not an option. This is not, frankly, the Bush administration, where they're going to issue a signing statement and refuse to enforce it. They will enforce it."

### *SEC Commissioner: Restoring Investor Trust a Key Goal*

Restoring investor confidence through corporate governance reforms must remain a priority for the Securities and Exchange Commission (SEC) during difficult economic times, an SEC commissioner said on Feb. 18.

"I have heard rumblings that this is not the time to divert our focus from the current market crisis and the need for regulatory reform by addressing other issues such as corporate governance," Commissioner Elisse Walter said. "I couldn't disagree more."

In a speech to the Practicing Law Institute, Walter identified several measures as being important to boosting the investor trust that has been lost in recent years, with proxy access first on the list.

"To me, the fundamental question is: 'Should shareholders have a real say in determining who will oversee management of the companies that they own,'" Walter said. "I believe strongly that the answer is yes."

After reviewing several of the proxy access reform measures that have been proposed recently, Walter said that the commission "needs to carefully consider a range of approaches."

Walter also stressed the importance of giving shareholders a voice on executive compensation issues. This, she said, would improve investor trust because it "promotes increased shareholder participation and increased accountability of board members and corporate management."

In addition, Walter discussed enhancing disclosures about director nominees, reexamining issues related to shareholder votes being cast through company Web sites ("e-proxy") and looking at uninstructed broker votes.

***Obama Outlines Financial Regulation Reform Plans***

President Obama on Feb. 25 identified seven broad principles for reforming regulation of the financial markets, including boosting transparency, recognizing the global nature of the problems and increasing accountability, "starting at the top."

Obama and many Democrats have frequently blamed many of the problems in the financial markets and the economy as a whole to inadequate government regulation.

"The choice we face is not between some oppressive government-run economy or a chaotic and unforgiving capitalism," Obama said. "Rather, strong financial markets require clear rules of the road, not to hinder financial institutions, but to protect consumers and investors, and ultimately to keep those financial institutions strong. Not to stifle, but to advance competition, growth and prosperity. And not just to manage crises, but to prevent crises from happening in the first place, by restoring accountability, transparency and trust in our financial markets."

Obama's reform outline also includes tightening oversight of institutions that present systemic risks, strengthening markets, supervising financial products based on "actual data" and eliminating gaps from regulations.

Some lawmakers – House Financial Services Committee Chairman Barney Frank, D-Mass., in particular – have talked of creating a "super-regulator" to oversee the markets and watch for "systemic" dangers that could, as happened recently, result in widespread collapse. The Federal Reserve has been mentioned as a candidate to assume the role. Obama did not address the this proposal.

Obama reportedly wants to make progress on regulatory reform before an April meeting of the world's 20 largest economies.

***Pension Reporting Rules Could Expand for CalPERS, Others***

Nestled into the middle of budgetary table on page 126 of the 10-year spending plan released by President Obama in late February is an indication that the administration wants to impose new reporting requirements on CalPERS and other state and local employers that do not participate in Social Security.

The table cites hundreds of millions of dollars in anticipated federal revenue starting in fiscal year 2013 coming from "Social Security Administration: Program integrity: require States and localities to provide pension information." This presumably refers to a planned attempt to enhance enforcement of the government pension offset and the windfall elimination provision, measures that reduce certain Social Security benefits for retirees who collect pensions from jobs that were not covered by the program.

From 2013-2019, the plan would reduce federal spending by $2.9 billion, a little over one-tenth of 1 percent of Obama's planned $2 trillion in budget savings over the next decade.

President Bush proposed a similar measure in his fiscal 2007 budget plan and threatened to penalize non-compliant employers by denying them access to IRS tax information. The proposal did not become law. It may not be known if Obama's plan includes a similar punishment until he releases his full 2010 budget in a few weeks.

Many critics have derided these proposals as attempts to impose unfunded mandates and have state and local agencies do work that should be done by the Social Security Administration.

### *Ex-CalPERS Official Named to Key SEC Post*

Former CalPERS general counsel Kayla Gillan has been named senior advisor to Securities and Exchange Commission (SEC) Chairman Mary Schapiro.

Gillan, who began in the new position on Feb. 17, left CalPERS after 16 years, including six as general counsel, to become a founding member of the Public Company Accounting Oversight Board in January 2003. The PCAOB, which Gillan left in January 2008, was created by the 2002 Sarbanes-Oxley Act, which reformed certain corporate governance and accounting rules and which CalPERS had a significant role in crafting.

Gillan is expected to help create an Investor Advisory Council at the SEC as well as work on other shareholder issues, such as matters related to proxy access and executive compensation. "I'm excited to have the opportunity to work with Chairman Schapiro, the commission and its staff as we work together to protect investors during these challenging times," Gillan said. "I'm eager to play tables a role in this great agency's self-evaluation and recommitment to meeting the needs of the investor community as well as the challenges posed by today's financial regulatory system."

## RELATED NATIONAL AND INDUSTRY NEWS

### *New Withholding Guidelines May Confuse Pension Funds*

New withholding that were issued by the IRS following enactment of the "Make Work Pay" tax credit may appear to apply to pension recipients, but they probably do not.

The credit, which was included in the economic stimulus bill, will reduce annual taxes by $400 for most individuals and $800 for most families. The Obama administration wants withholding to change as soon as possible so that taxpayers can start getting the money immediately, rather than waiting until they file their tax returns in early 2010.

It is unclear in the IRS guidelines, though, whether employers should use the new tables for their pensioners. In response to an inquiry from CalPERS Federal Representative Lussier, Gregor, Vienna and Associates, a Treasury Department official acknowledged that, "read literally," the new guidance seems to indicate that pension payments should be adjusted according to the new tables. But pensions are not considered to be "earned income" for the purposes of the tax credit, he added, and, thus, are likely not eligible for the benefit. So, "using the new tables will increase the likelihood that pension recipients will owe taxes (and possibly penalties) at the end of the year." The official said the IRS would provide additional information.

In a related matter, retirees who worked in jobs not covered by Social Security will receive a one-time payment of $250 in lieu of the "Make Work Pay" credit. In early versions of the stimulus legislation, the $250 benefit was to be provided only to retirees who participated in Social Security, but Congress approved an amendment offered by Sen. John Kerry, D-Mass., that extended the benefit to all retirees.

CalPERS Federal Representative Lussier, Gregor, Vienna & Associates worked closely with Kerry's office to guarantee equal treatment in the bill for public retirees who are outside of Social Security.

***Commodities Investments OK for Pension Funds, GAO Concludes***

Institutional investors have not acted inappropriately by putting a portion of their funds in commodities indexes, a report released Jan. 30 by the Government Accountability Office (GAO) concluded.

Prices for commodities, such as crude oil and wheat, rose for several years through mid-2008, a trend that some attributed, at least in part, to investments in commodities indexes, the report noted. Pension funds and other institutional investors have bought into such indexes for a few years, and the GAO sought to determine the propriety of these investments.

In its report, the GAO not only concluded that institutional investors have acted legally, but noted that Commodity Futures Trading Commission staff determined that "the use of the futures markets by [institutional] funds to provide their investors with a commodity-index exposure represented a legitimate and potentially useful investment strategy."

The GAO report echoes the position that CalPERS took during a debate on this subject in 2008.

***Neas Named CEO of NCHC***

Ralph Neas, one of the most effective and best known activists in Washington, has been named chief executive officer of the National Coalition on Health Care (NCHC).

"To be selected as the new CEO is an honor and an extraordinary opportunity," Neas said. "It's imperative that the administration and Congress reform the nation's health care system in 2009; failure to do so risks causing untold damage to the national economy and our citizens."

Neas had served as president and CEO of People for the American Way (PFAW). Throughout his career, he has been particularly active on civil rights and civil liberties issues, the primary focus of PFAW.

NCHC also recently announced that former Democratic congressman Bob Edgar, the chairman and CEO of Common Cause, has been named a new coalition co-chair.

CalPERS is an active member of NCHC, with CalPERS Board Member George Diehr serving on the coalition's board of directors.

## CALIFORNIA CONGRESSIONAL DELEGATION NEWS

### *Solis Confirmed as Labor Secretary*

After weeks of delay, the Senate on Feb. 24 confirmed Rep. Hilda Solis, D-Calif., to be secretary of the Department of Labor.

Solis' nomination was first delayed by a dispute over whether her work as the unpaid treasurer for American Rights at Work, an advocacy group that supports the ability of workers to form unions, amounted to lobbying. It was then put on hold after revelations that her husband had only recently paid $6,400 to settle tax liens – some going back 16 years – related to an auto repair business that he owned. White House officials insisted that Solis was not involved in the business and was not aware of the tax issues. Her husband reportedly plans to challenge the validity of the liens.

Solis was confirmed by a vote of 80-17.